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Newfoundland Telephone Company Limited

Annual Report 1978

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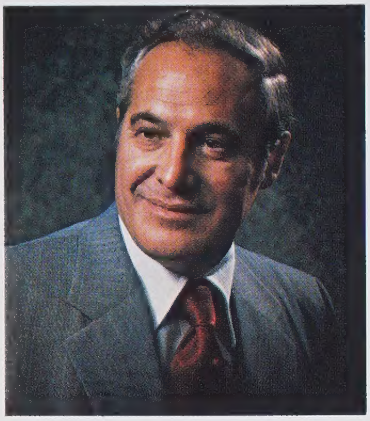


A.A. Brait
President and Chief Executive Officer

President's Message

The past year marked the culmination of many activities which have served to strengthen the organization and strike that essential balance in the Company's operations which produces good, low cost service for our customers, attractive financial returns for our shareholders and satisfying careers for our employees. The Company has met the challenges of changing customer demand under changing economic and business conditions through the timely introduction of new technology and service improvement programs, new marketing approaches, consolidation of operations and continued emphasis on sound financial management and performance.

During the year construction of a microwave system connecting all parts of our operating territory was completed. New data and video communication services were introduced to serve our business customers. In addition, we completed a major improvement program in Labrador bringing service in that area of the province up to the standard enjoyed on the Island. In December, we opened our first Phonecentre, a new concept in the marketing of telephone services which will also improve the efficiency of telephone installations. In 1978 as well, two important projects designed to consolidate our operations were initiated. An agreement reached with the Iron Ore Company of Canada to acquire the telephone system in Labrador City will extend our serving territory to include all of Labrador. And, in the spring of 1979 we will commence construction on a new head office administration building in St. John's.

The Company's financial performance continues to be strong. Earnings increased during 1978 and improvements were achieved in all financial indicators. This was reflected in the strong investor confidence evident throughout the year. A common equity issue in October was well received and, in addition to generating needed capital, served to broaden the ownership base of the Company. The notable achievements of the past year are recorded in the Report of the Directors.

The continuing advances within the industry have created a challenging work environment and enabled us to attract highly qualified personnel. In addition, the advantages of the new organization adopted by the Company some eighteen months ago were evident in the improved effectiveness of our operation throughout 1978. The developments and successes of the past year are, to a large degree, due to the dedicated efforts and resourcefulness of our employees.

It is particularly satisfying that during a period of continuing inflationary pressures, these advances have been possible without the necessity of having to impose a general rate increase on our customers. The Company has continued to provide a high quality service at reasonable cost.

The future of the telecommunication industry looks bright as demands for communication services continue to increase. This, together with the prospects of an improving provincial economy, provides your Company with the opportunity for continued advances in 1979 and beyond. We are confident that building on the balanced performance achieved in 1978, we can take full advantage of these opportunities.

A.A. Brait

Report of the Directors

Balanced development is an essential element in the ongoing success of any business enterprise. During 1978 a number of programs were completed which allowed the Company to match technological advances with customer demands for new and improved services. Steps were also taken to consolidate operations both in Labrador and on the Island and to bring levels of service in both areas of the province up to the same standard. The achievement of a balanced financial structure and a growth in earnings were two important results of a continuing emphasis to improve all areas of financial performance. Taken together, these developments have contributed to making 1978 one of the most successful years in your Company's history.

Financial Performance

Earnings per average common share in 1978 were $1.17, an increase of 10.4 percent over 1977. The rate of return on average total capital for the year was 11.16 percent compared to 10.92 percent in the previous year.

The Company's strong earnings performance in 1978 resulted mainly from a high growth in long distance revenues, particularly during the last six months. Disruptions in the country's postal and airline services had a positive impact on revenues in this period. However, to a large degree, this revenue growth reflects the increased use of telecommunication services by our customers.

By the fourth quarter of the year, the Company had determined that with this accelerated revenue growth, 1978 earnings would exceed the allowable rate of return on average common equity of 14.50 percent as established under the regulations of the Anti-Inflation Act and administered by the Public Utilities Board of Newfoundland. As a result, the Company submitted to the Board a plan to reduce long distance rates by an average of eight percent for calls within the province. This submission was approved and the reduction became effective on December 1, 1978. In addition, the Public Utilities Board approved a plan to defer excess 1978 earnings and carry them forward as earned income into the following fiscal year. This will enable the Company to make positive use of the strong financial performance for the future benefit of telephone subscribers. The Company's rate of return on average common equity for the year was 14.50 percent. This compares to 14.27 percent for the previous year.

In August, the Company declared a third-quarter dividend of $0.175 per common share. This indicated an annual dividend rate of $0.70, an increase of $0.10 per share. This decision is significant to investors as it underlines the Company's intention of paying dividends, subject to earnings performance, which are designed to keep pace with inflation.

In October, the Company welcomed approximately 1,000 new shareholders when it completed its second public common share offering with the issue of 1.2 million shares at a price of $10.125 per share. The proceeds of this issue were used to finance part of the Company's construction program. A significant result of this issue was the realization of a debt/equity ratio of approximately 50 percent. This balanced capital structure will provide the Company with financing flexibility when future external financing is required.

The market price of the Company's shares at year end was $10.375, compared to $8.50 at the same date in 1977.

Our ability to generate 57 percent of our total capital requirements from internal sources is encouraging and is another indicator of a strong financial performance in 1978.

Technology and Service Improvements

The Company invested $27.3 million in 1978 to construct and modernize facilities and to provide the quality and variety of services required by residential and business customers.

During the year the Company completed construction of its provincial microwave network.

One of the Company's most important technological advancements of recent years was realized in July with the completion of a provincial microwave system. The system provides a direct, high quality telecommunication system linking all parts of the Company's operating territory in Newfoundland and Labrador.

Another key advancement was made this year with the completion of the Labrador Improvement Program. In addition to the construction of a new microwave system, all outside cable facilities on the south coast of Labrador were rebuilt. These improvements have provided for the introduction of Direct Distance Dialing (DDD) to most centres. As well, local calling capabilities were improved with the introduction of Extended Area Service (EAS) to a number of coastal communities. Labrador subscribers now have the same quality of service as our Island customers. Almost 100 percent of our customers now enjoy both private line and DDD service, the best such record in Canada.

Newfoundland Telephone serves approximately 70 percent of the residents of Newfoundland and Labrador.

In August, a $2.5 million expansion was completed at the Mount Pearl Exchange Building near St. John's. The building was expanded and a modern electronic switching machine installed to handle the growth requirements of the area.

In November, construction was completed on a new exchange building for Grand Falls. The new building will house an electronic switching system as well as a new business office which will serve the central Newfoundland area. Completion of the $6.0 million project is scheduled for mid-1979.

At year end, the Company had a total investment in plant and equipment of $234,300,000 or $1,300 per telephone in service.

These advances in technology have made it possible for the Company to offer a wider range of telecommunication services to both business and residential customers. In response to increasing customer demand from both sectors, the Company has been able to enter expanded revenue producing markets through the employment of new marketing techniques and the introduction of specialized services.

In July, the Company introduced Omnidata, Newfoundland's first provincial data network. Omnidata provides the province's data users with a top quality, low cost transmission service which can be tailored to meet individual customer needs.

A new data information system for the Provincial Government, connecting 32 locations, was implemented during the year as well as new data systems for several other business customers.

Significant achievements were also made in the field of broadcast communication services. The Canadian Broadcasting Corporation's television and AM/FM radio networks, as well as a privately owned provincial FM radio network, were brought onto our microwave system.

Because of the rapid growth in special services, the Company established a Special Services Operations Centre in June at the Allandale Exchange in St. John's. This operation provides a central point from which these services can be monitored and tested, thereby minimizing service disruption.

New SL-1 electronic switchboards were introduced to the Company's product line during 1978 and installations completed in two St. John's hospitals. This equipment allows more direct access to these key institutions.

New concepts were also evident in the marketing of telephone service to residential customers when, in December, the Company opened its first Phonecentre in St. John's. Through the use of pre-installed jacks at subscribers' residences, customers can visit Phonecentre, choose their telephone and complete their own service installation. By year end approximately 25 percent of the homes in the St. John's area had been provided with the special telephone outlets which permit the easy plug-in installation. The conversion will be completed by the end of 1979. The new service, which has been well received by our customers, will improve installation efficiency and strengthen our marketing thrust in the residential market.

In 1978, 10,499 telephones were added to the system, bringing total telephones in service to 175,312. This net gain in telephones is nearly double the previous year's figure. Long distance messages increased by 13.2 percent over 1977 to approximately 14.8 million. These statistics indicate an expanding use of telecommunication services by various sectors of the economy.

Consolidation

The Company has taken an important step to consolidate its operations in reaching agreement with the Iron Ore Company of Canada to purchase their telecommunication system in Labrador City which comprises about 6,500 telephones.

An artist's conception of the Company's new head office building.

The acquisition, which is expected to be finalized in early 1979, will almost double our telephone base in Labrador. More importantly, it will mean that the entire Labrador region will now be served by the Company. This will contribute to the increased efficiency of our operations in the area.

During the year, the Company announced plans for the construction of a new headquarters administration building in St. John's. The six-storey complex will bring together under one roof some 700 employees presently in various locations throughout the city. The building is to be located in the downtown area of St. John's and is designed to complement the unique architecture of this historic area. Construction is scheduled to begin in the spring of 1979 and to be completed in 1981.

In December, the Company entered into an agreement with the Eastern Telephone and Telegraph Company (E.T.&T.) and its parent, the American Telephone and Telegraph Company (A.T.&T.) for the provision of certain telecommunication services at Clarenville, in eastern Newfoundland. Under the agreement the Company acquired the cable terminal building associated with E.T.&T.'s trans-Atlantic cable operation and contracted to operate the cable station until 1982. The agreement further provided for the use of Company-supplied transmission facilities between eastern Newfoundland and the other Atlantic provinces.

Regulation

In its order dated December 19, 1978, the Board of Commissioners of Public Utilities of Newfoundland approved the Company's application to align basic local service rates in Labrador with those of the Island. The new rates become effective February 1, 1979. The Board's decision indicates a recognition that the same level of service now exists throughout our operating territory.

Earlier in the year, the Board granted approval for a change in the Company's method of calculating depreciation rates on station equipment. The method used is now consistent with the depreciation of all other Company assets resulting in a more equitable recovery of capital costs.

Organizational Development

Newfoundland Telephone employed 1,475 people at year end. Wages and salaries paid in 1978 totalled $20,193,000 and benefits and pension fund contributions amounted to $2,105,000.

1978 marked the completion of the first full year of operation under the new "work flow" organization adopted in late 1977. A departure

from the traditional organization which groups employees of similar skills, this approach realigns employees according to similar work functions. This organizational structure has been instrumental in enabling our employees to record the impressive achievements of the past year.

The rapid expansion in technology and service has increased the need for employee training. In keeping with this requirement, the Company has provided its personnel with the most up-to-date training available in the telecommunication industry. During 1978 comprehensive training courses were carried out in the areas of both management skills and technical development. These will continue to be an integral part of our employee development program.

In November, the Company announced certain changes to its pension plan. Included in the changes was the introduction of a new eligibility criterion providing for increased flexibility with regard to retirement prior to age 65. The introduction of a supplemental pension provision was also included.

Two collective agreements, covering almost 600 employees, were signed in 1978 with the International Brotherhood of Electrical Workers, Local 1615. The first, signed on March 23 covering 182 telephone operators, is a two-year agreement scheduled to expire on February 29, 1980. This contract contains a wage reopener clause in the second year. In addition, the Company concluded a one-year agreement on May 1 covering about 400 craft employees, including installers, splicers, linemen and maintenance personnel. This contract expires on March 31, 1979. Both agreements were within the guidelines established by the Anti-Inflation Board for the third year of the program.

In December, the Company opened its first Phonecentre in St. John's.

Board of Directors

The Board of Directors welcomed two new members during 1978, both of whom bring considerable business knowledge and experience to the Board. Mr. D.W. Clark was elected to the Board at the 1978 Annual General Meeting of Shareholders on March 29. Mr. Clark is President and General Manager of Bowater Newfoundland Limited, a pulp and paper company located in Corner Brook. Mr. D.D. Munro, Resident General Manager of Price (Nfld.) Pulp & Paper Limited in Grand Falls, was appointed to the Board on August 23 to fill the vacancy left by the resignation of Mr. M.T. Neill, who is now residing in Toronto. The Board wishes to express its appreciation for Mr. Neill's contribution to the Company during his three and one-half years' service on the Board.

As the Company has expanded over the past few years, the role of the Board's committees has increased in importance. The Board utilizes two such committees; the Audit Committee and the Resource Committee. Their mandate is to review specific matters of importance in greater detail and make related recommendations to the Board. The Audit Committee has the major task of reviewing and approving the Company's financial statements, accounting procedures and all audit oriented matters. The Resource Committee is largely responsible for personnel administration matters and the Company's salary administration plan.

Outlook

The outlook for the provincial economy in 1979 is positive. The fishery, the province's largest industry, is expected to continue its recent expansion while oil and gas exploration off the Labrador coast will be accelerated. Mining exploration is increasing and with this activity the industry should regain its former strength and stability. Preparation will continue next year for the start of a new pulp and paper operation on the Island's west coast, and for the renewed operation of an oil refinery on the east coast.

With the projected upturn in the provincial economy, we can expect demands for diverse, sophisticated telecommunication services to grow. We are confident that the advances of the past year will put us in an ideal position to take advantage of these new opportunities.

In addition, growth and modernization of our facilities will continue in 1979 consistent with the Company's objective of utilizing the most advanced technologies to meet our customers' needs. Construction expenditures are expected to reach $32 million. TOPS (Traffic Operator Position System), a computer-based system to improve long distance call handling and billing efficiency, will be introduced during the year. Construction of the new Grand Falls exchange will be completed and construction of the Company's new head office will commence. Our new microwave network will provide the basis for the expansion of new services to all areas of our operations. Telephone gain is forecast to reach approximately 10,000.

The telecommunication industry continues to grow and offers an excellent opportunity for the investor. During 1978 Newfoundland Telephone has put in place the elements which are essential for continued advancement. We look forward to the future with optimism.

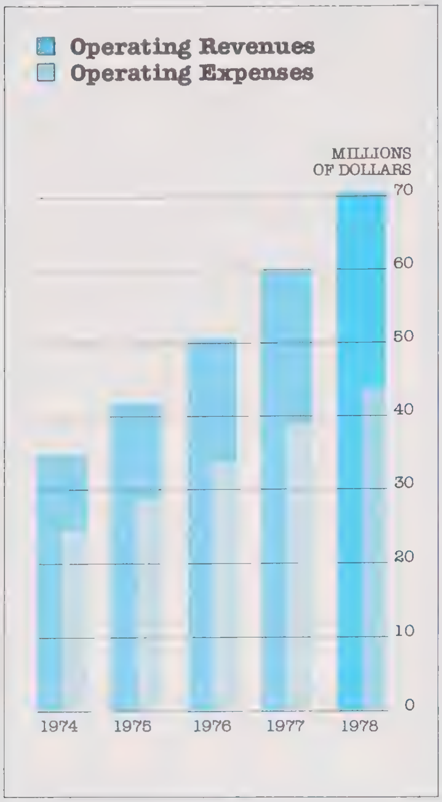
A.A. Brait

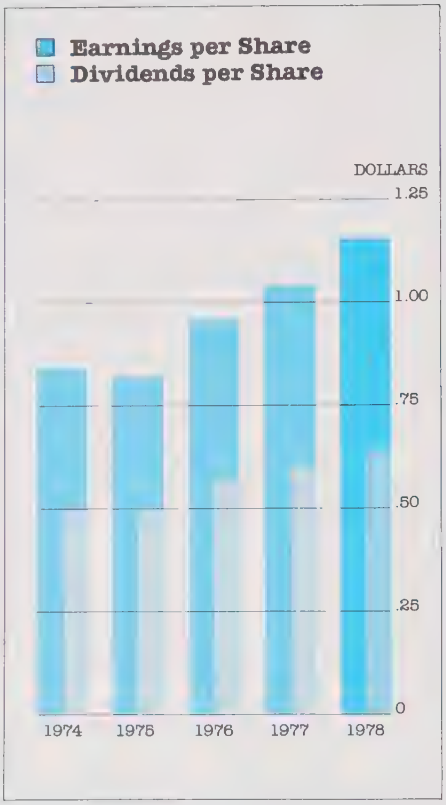
A.A. Brait
President and Chief Executive Officer
February 8, 1979.

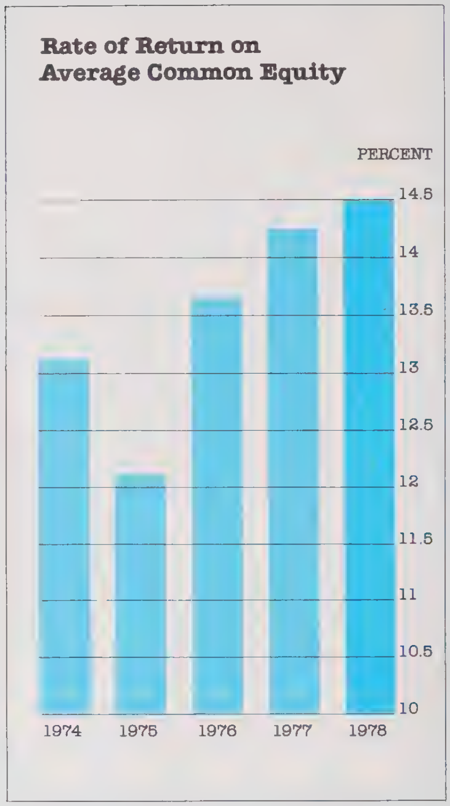
Financial and Corporate Information

Operating and Financial Statistics

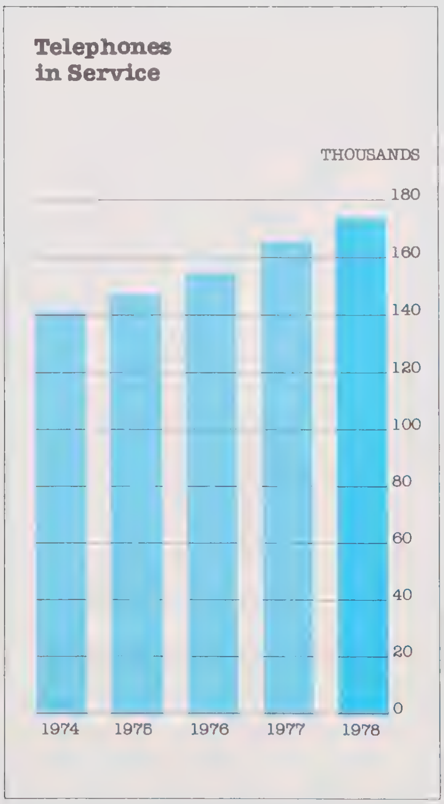
FINANCIAL

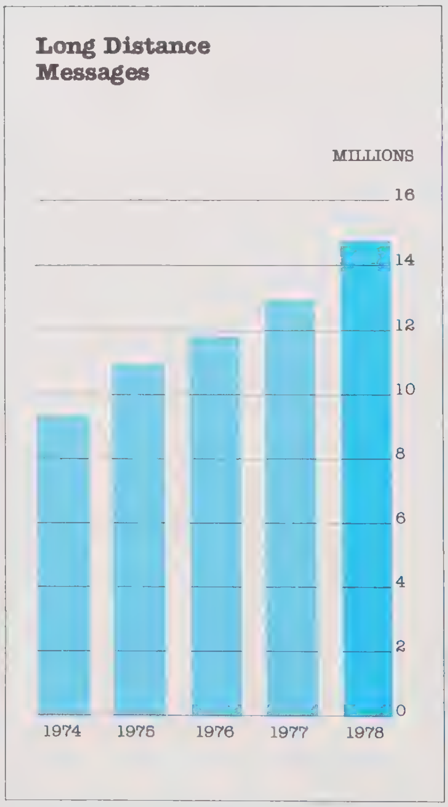


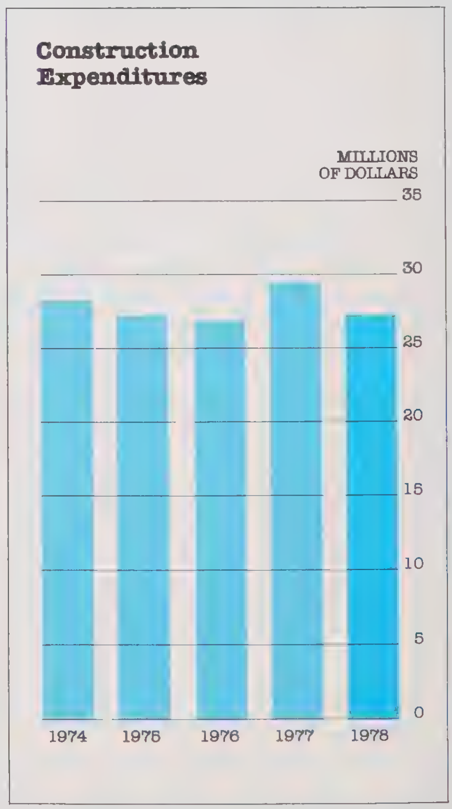




OPERATIONS



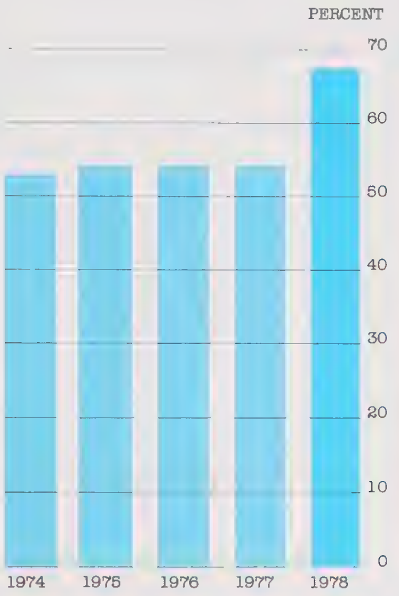




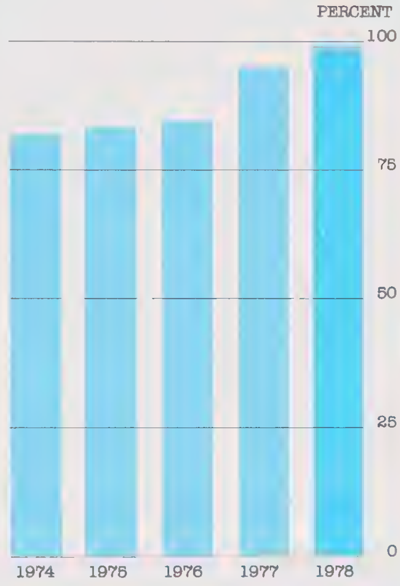
Service and Technology Statistics

SERVICE

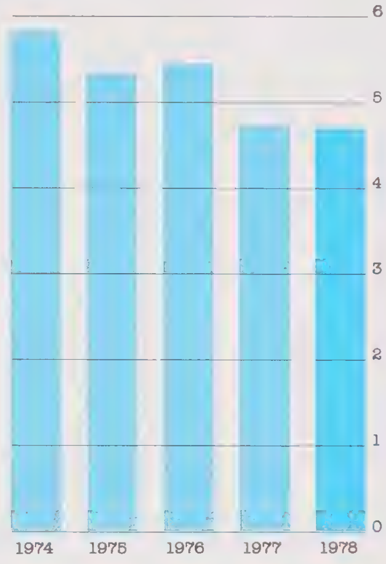
% Telephones with Automatic Number Identification



Direct Distance Dialing

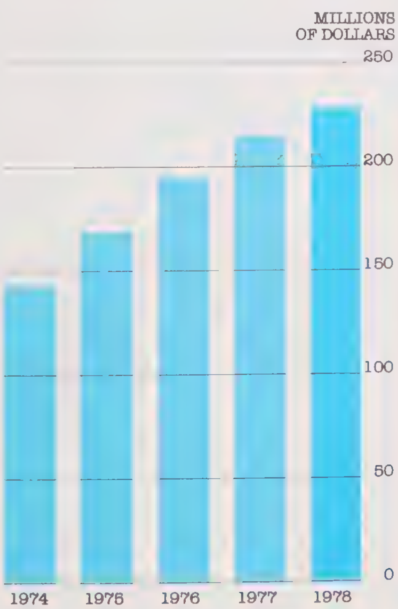


Average Number of Service Troubles per 100 Telephones

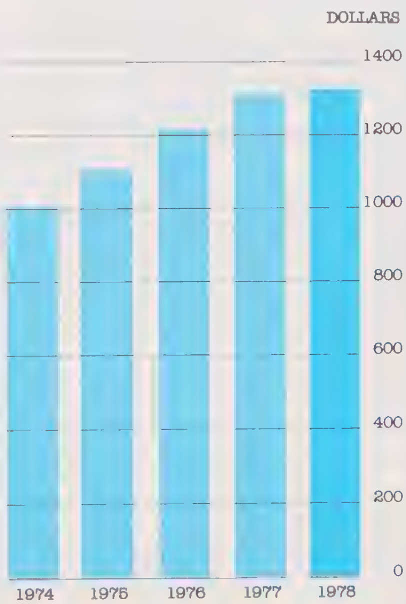


TECHNOLOGY

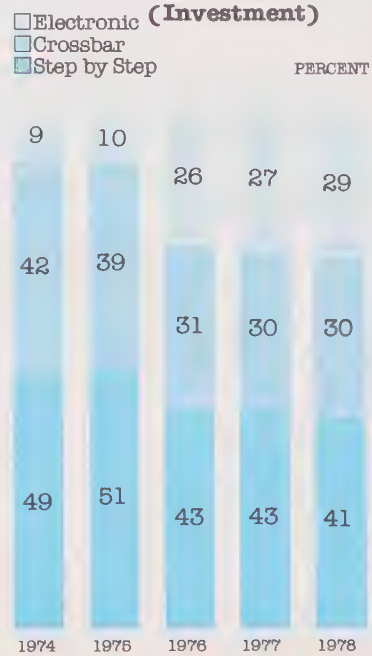
Telephone Plant and Equipment



Total Investment per Telephone



Central Office Switching by Type of Technology (Investment)



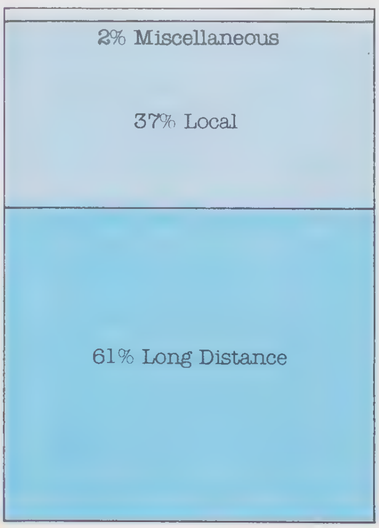
1978 Financial Highlights

	Year 1978	Year 1977	Changes
Revenues			
Local service	$26,245,928	$23,011,960	$ 3,233,968
Long distance service	43,556,959	36,750,013	6,806,946
Miscellaneous income-net	1,371,993	700,299	671,694
Total revenues	71,174,880	60,462,272	10,712,608
Expenses			
Operating expenses	44,360,255	39,349,285	5,010,970
Income taxes	7,536,014	4,940,361	2,595,653
Interest charges	8,488,798	7,591,806	896,992
Total expenses	60,385,067	51,881,452	8,503,615
Net Income before Transfer	10,789,813	8,580,820	2,208,993
Transfer	943,175	–	943,175
Net Income	$ 9,846,638	$ 8,580,820	$ 1,265,818

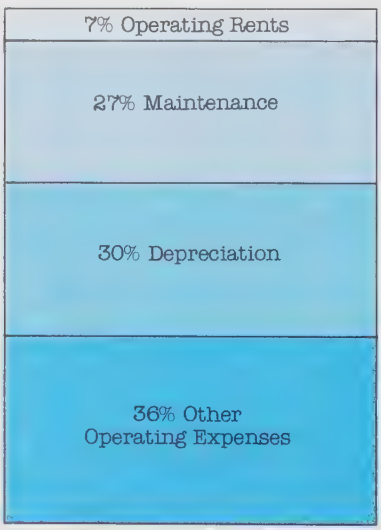
Financial Results:

Total revenues increased by 17.7%
Total expenses increased by 16.4%
Construction expenditures amounted to $27,334,446
Investment in plant and equipment reached $234,345,123
Rate of return on average total capital was 11.16%
Rate of return on average common equity was 14.50%
Dividends paid per common share were $0.65

Breakdown of Operating Revenues 1978



Breakdown of Operating Expenses 1978



Income Statement

	Year 1978	Year 1977
Operating Revenues		
Local service	$ 26,245,928	$ 23,011,960
Long distance service	43,556,959	36,750,013
Miscellaneous – net	703,890	409,030
Total Operating Revenues	70,506,777	60,171,003
Operating Expenses		
Depreciation (Notes 1 and 2)	13,138,268	11,710,587
Maintenance	12,044,521	10,363,610
Operating rents	2,985,806	2,979,856
Other operating expenses	16,191,660	14,295,232
Total Operating Expenses	44,360,255	39,349,285
Net Operating Revenues	26,146,522	20,821,718
Other Income (Note 8)	668,103	291,269
Income Before Underlisted Items	26,814,625	21,112,987
Interest Charges		
Interest on long term debt	7,728,944	5,996,749
Other interest	759,854	1,595,057
Total Interest Charges	8,488,798	7,591,806
Income Before Income Taxes	18,325,827	13,521,181
Income Taxes (Notes 1 and 7)	7,536,014	4,940,361
Net Income Before Transfer	10,789,813	8,580,820
Transfer To Deferred Income (Note 12)	943,175	–
Net Income	9,846,638	8,580,820
Dividends on Preferred Shares	1,984,268	1,740,813
Net Income Applicable to Common Shares	$ 7,862,370	$ 6,840,007
Earnings Per Common Share (based on average number of shares outstanding)	$1.17	$1.06

Balance Sheet

ASSETS	December 31 1978	December 31 1977
Telecommunication Property		
Buildings, plant and equipment – at cost	$224,517,416	$202,950,652
Less: Accumulated depreciation (Notes 1 and 2)	63,347,632	53,141,562
	161,169,784	149,809,090
Land and plant under construction – at cost	9,827,707	9,866,528
Materials and supplies (Note 1)	3,686,931	3,405,879
	174,684,422	163,081,497
Investment – Shares in Telesat Canada – at cost	300,000	300,000
Current Assets		
Short term investments – at cost	5,862,405	7,000,000
Accounts receivable – principally from customers	11,063,294	8,943,379
Prepayments	602,116	508,108
	17,527,815	16,451,487
Deferred Charges		
Unamortized deficiency in accumulated depreciation (Notes 1 and 2)	674,325	749,251
Unamortized long term debt expenses (Note 1)	1,347,715	1,419,568
Other (Note 1)	1,875,918	654,360
	3,897,958	2,823,179
	$196,410,195	$182,656,163

On behalf of the Board of Directors:
F. O'Dea, Q.C., Director
H. Collingwood, Director

LIABILITIES AND SHAREHOLDERS' EQUITY	December 31 1978	December 31 1977
Shareholders' Equity		
Capital stock (Note 3)		
Preferred shares	$ 22,223,000	$ 22,696,800
Common shares	46,661,295	34,511,295
Premium on common shares	775,987	775,987
Capital redemption reserve fund (Note 3)	1,777,000	1,303,200
Retained earnings	15,047,806	12,659,883
	86,485,088	71,947,165
Unsecured Subordinated Notes – Due to Parent Company (Note 4)	6,259,941	7,389,941
Long Term Debt (Note 5)	79,512,000	81,478,000
Notes Payable (Note 6)	–	2,900,000
Current Liabilities		
Bank advance	3,707,853	1,218,310
Accounts payable	3,735,656	2,483,828
Due to parent company	168,207	134,219
Due to affiliated companies	785,561	2,703,007
Advance billing for service	971,218	806,841
Taxes accrued	2,771,571	2,474,254
Interest accrued	1,422,344	1,422,880
Dividends payable	83,444	86,162
Deferred income (Note 12)	943,175	–
	14,589,029	11,329,501
Deferred Income Taxes (Notes 1 and 7)	9,564,137	7,611,556
	$196,410,195	$182,656,163

R.H. Benson, Comptroller

Statement of Retained Earnings

	Year 1978	Year 1977
Balance at Beginning of Year	$ 12,659,883	$ 10,292,703
Net Income	9,846,638	8,580,820
	22,506,521	18,873,523
Deduct:		
Dividends		
Preferred shares	1,984,268	1,740,813
Common shares	4,423,468	3,889,355
	6,407,736	5,630,168
Transfers to capital redemption reserve fund	473,800	284,360
Expenses on issues of capital stock (net of income tax of $180,641; 1977 – $126,612)	577,179	299,112
	7,458,715	6,213,640
Balance at End of Year	$ 15,047,806	$ 12,659,883

Statement of Changes in Financial Position

Source of Funds	Year 1978	Year 1977
Operations		
Net income	$ 9,846,638	$ 8,580,820
Items not requiring current funds		
Depreciation and miscellaneous	13,134,369	11,748,119
Deferred income taxes	1,931,391	1,954,210
	24,912,398	22,283,149
Proceeds from issue of preferred shares	–	9,574,276
Proceeds from issue of common shares	11,392,180	–
Proceeds from issue of long term debt	–	19,584,500
Decrease in working capital	2,183,200	–
Miscellaneous	474,839	316,017
	$ 38,962,617	$ 51,757,942

Disposition of Funds	Year 1978	Year 1977
Construction expenditures		
Gross construction expenditures	$ 27,334,446	$ 29,758,135
Deduct: Charges to construction not requiring an outlay of funds	(1,530,417)	(810,277)
Increase in materials and supplies	281,052	60,512
	26,085,081	29,008,370
Dividends – Preferred	1,984,268	1,740,813
– Common	4,423,468	3,889,355
Redemption of preferred shares	473,800	284,360
Repayment of subordinated notes	1,130,000	1,130,000
Repayment of long term debt	1,966,000	1,716,000
Net repayment of notes payable	2,900,000	8,500,000
Increase in working capital	–	5,489,044
	$ 38,962,617	$ 51,757,942

The increase (decrease) in working capital is accounted for by:	Year 1978	Year 1977
Increase (decrease) in current assets:		
Short term investments	$ (1,137,595)	$ 7,000,000
Accounts receivable	2,119,915	1,777,629
Prepayments	94,008	(244,746)
(Increase) decrease in current liabilities:		
Bank advance	(2,489,543)	(330,822)
Accounts payable	(1,251,828)	(227,307)
Due to parent company	(33,988)	234,565
Due to affiliated companies	1,917,446	(2,310,985)
Advance billing for service	(164,377)	(144,999)
Taxes accrued	(297,317)	(137,461)
Interest accrued	536	(90,470)
Dividends payable	2,718	(36,360)
Deferred income	(943,175)	–
	$ (2,183,200)	$ 5,489,044

Notes to Financial Statements

1. Accounting Policies

The accompanying financial statements, which were approved by management on February 8, 1979, have been prepared in accordance with generally accepted accounting principles.

The Company is subject to regulation, including examination of accounting practices, by the Board of Commissioners of Public Utilities of Newfoundland ("Board of Commissioners"). The system of accounts and accounting practices are similar to those being used in the telecommunication industry except as described in Note 7 with respect to accounting for income taxes.

Depreciation

Depreciation is computed on the straight line method using rates based on the estimated useful lives of the assets. When depreciable telecommunication property is retired, the amount at which such property has been carried in telecommunication property is charged to accumulated depreciation (See Note 2).

Income Taxes

Tax allocation accounting has been followed with respect to timing differences other than those related to differences between capital cost allowances and depreciation (See Note 7).

Materials and Supplies

Materials and supplies consist of items which will be used in the construction program and are valued principally at average cost.

Deferred Charges

Expenses incurred for other than long term debt are being amortized as ordered by the Board of Commissioners (See Note 2). Expenses incurred in connection with the issue of long term debt are amortized on a straight line basis over the life of the debt.

2. Depreciation

Commencing July 1, 1966 the provision for depreciation has been accumulated at rates for each class of plant determined by the Company's engineers and approved by the Board of Commissioners. Prior to July 1, 1966 depreciation was provided in varying amounts, not exceeding the rate of 3.3%, approved by the Board of Commissioners on January 14, 1952, which resulted in an accumulated depreciation deficiency as at June 30, 1966 estimated at $3,390,000.

Effective January 1, 1967 the Company began to amortize the accumulated depreciation deficiency at the rate of $170,000 per annum. This amortization was subsequently cancelled by the Board of Commissioners by its Order No. 6 dated March 27, 1968, ordering the Company to account for the accumulated depreciation deficiency in the following manner:

1) a charge against retained earnings	$ 218,500
2) the elimination of the deferred credits-income tax as of June 30, 1966	1,673,000
3) the setting up of the remaining amount in a special account which is being amortized over a period of 20 years commencing on January 1, 1968	1,498,500
	$3,390,000

The depreciation expense for the year ended December 31, 1978 was $13,138,268 (1977 – $11,710,587) and the composite rate was 6.29% (1977 – 6.40%).

3. Capital Stock

Authorized

250,000	7.25% cumulative redeemable preferred shares of the par value of $20 each
450,000	9.75% cumulative redeemable preferred shares of the par value of $20 each
500,000	8.85% cumulative redeemable preferred shares, Series C of the par value of $20 each
9,000,000	common shares without par value

Outstanding		December 31 1978	1977
215,150	7.25% preferred shares (1977 – 220,840 shares)	$ 4,303,000	$ 4,416,800
396,000	9.75% preferred shares (1977 – 414,000 shares)	7,920,000	8,280,000
500,000	8.85% preferred shares, Series C (1977 – 500,000 shares)	10,000,000	10,000,000
		$22,223,000	$22,696,800
7,682,259	common shares (1977 – 6,482,259 shares)	$46,661,295	$34,511,295

On April 25, 1977 the Company issued 500,000, 8.85% cumulative redeemable preferred shares, Series C of the par value of $20 each.

On October 13, 1978 the Company issued for cash 1,200,000 common shares without par value at a price of $10.125 per share.

The 7.25% cumulative redeemable preferred shares may be redeemed at the Company's option in whole or in part for a redemption price of $21.00 if redeemed on or before September 15, 1981, $20.80 thereafter to September 15, 1984, $20.60 thereafter to September 15, 1987, $20.40 thereafter to September 15, 1990 and $20.20 thereafter.

The 9.75% cumulative redeemable preferred shares are not redeemable prior to May 15, 1980 other than for sinking fund purposes but may be redeemed thereafter at the Company's option in whole or in part for a redemption price of $21.40 if redeemed on or before May 15, 1983, $21.20 thereafter to May 15, 1986, $21.00 thereafter to May 15, 1989, $20.80 thereafter to May 15, 1992, $20.60 thereafter to May 15, 1995, $20.40 thereafter to May 15, 1998 and $20.20 thereafter.

The 8.85% cumulative redeemable preferred shares, Series C are not redeemable prior to April 15, 1982 but may be redeemed thereafter at the Company's option in whole or in part for a redemption price of $21.20 if redeemed on or before April 15, 1985, $21.00 thereafter to April 15, 1988, $20.80 thereafter to April 15, 1991, $20.60 thereafter to April 15, 1994, $20.40 thereafter to April 15, 1997 and $20.20 thereafter.

During the year ended December 31, 1978, 5,690 of the 7.25% preferred shares of the aggregate par value of $113,800 and 18,000 of the 9.75% preferred shares of the aggregate par value of $360,000 were purchased for cancellation pursuant to the provisions attaching to these preferred shares. As required by The Companies Act (Newfoundland), equal amounts have been transferred from retained earnings to the "capital redemption reserve fund".

4. Unsecured Subordinated Notes – Due to Parent Company

Series A Unsecured Subordinated Notes – These notes of $5,650,000 (1977-$6,780,000) payable to Bell Canada bear interest at ¼ of 1% above a Canadian chartered bank's prime rate subject to a minimum annual rate of 7% and a maximum annual rate of 9%. These notes mature in equal amounts serially in each of the years ending December 31, 1979 to 1983 inclusive.

Series B Unsecured Subordinated Note – This note of $609,941 (1977-$609,941) payable to Bell Canada under the same interest conditions set forth for subordinated notes "A" matures on December 31, 1983.

These notes are redeemable at par without penalty at the option of the Company.

5. Long Term Debt

Series	Maturity	Issued	Outstanding
First Mortgage Sinking Fund Bonds			
6%	June 1, 1979	$ 1,000,000 (A)	$ 820,000
7%	May 1, 1980	2,000,000 (A)	1,660,000
9¼%	May 15, 1990	7,500,000 (A)	1,182,000
8⅝%	April 15, 1992	7,500,000 (A)	6,350,000
9%	December 1, 1994	15,000,000 (A)	13,500,000
11½%	February 1, 1996	10,000,000 (A)	10,000,000
11%	October 1, 1996	17,500,000 (A) (B)	17,500,000
			51,012,000
First Mortgage Bonds			
5½%	June 1, 1988	3,000,000	3,000,000
7%	December 15, 1991	3,000,000	3,000,000
7⅞%	November 1, 1993	2,500,000	2,500,000
9.85%	December 1, 1997	20,000,000	20,000,000
			$79,512,000

(A) Each of the seven series of First Mortgage Sinking Fund Bonds has a sinking fund requiring payment by the Company as follows:

(i) Series 6% and 7% require payment in each year of an amount equal to 1% of the issued aggregate principal amount of each such series.

(ii) Series 8⅝% and 9% require payment in each year commencing 1972 and 1974 respectively of an amount equal to 2% of the issued aggregate principal amount of each such series.

(iii) Series 9¼% and 11% require payment in each year commencing 1975 and 1979 respectively of an amount equal to 2% of (a) the issued aggregate principal amount of each such series less (b) the aggregate principal amount of each such series which has been or will be prepaid at the option of the holders thereof on May 15, 1975 and April 1, 1979, respectively.

(iv) Series 11½% requires payment in each year commencing 1982 of an amount equal to 5.7% of the issued aggregate principal amount of the series.

The aggregate amount of payments required in each of the next five years to meet maturities and sinking fund requirements of those series of First Mortgage Bonds of the Company presently outstanding is as follows: $1,540,000 in 1979, $2,440,000 in 1980, $800,000 in 1981, $1,388,600 in 1982 and $1,397,700 in 1983.

(B) The holders of any series 11% Bonds have the right to elect that the Company prepay the principal amount of the Bond on October 1, 1979 provided they present the Bonds to the Trustee after October 1, 1978 and prior to April 1, 1979 for notation.

6. Notes Payable

Demand bank loans (unsecured) outstanding bear interest at a Canadian chartered bank's prime rate, and represent interim financing incurred in the expansion of the Company's operations.

7. Income Taxes

The Board of Commissioners gave its approval commencing in 1973 to the use by the Company of the tax allocation basis of accounting for income taxes for timing differences other than those related to differences between capital cost allowances and depreciation. Previously the Company was not permitted to use tax allocation accounting.

Accordingly, since 1973 the Company has provided, as a current operating expense, deferred income taxes on those charges, other than capital cost allowances, which have been expensed for tax purposes but have not yet been charged against income in the financial statements.

As a result of not being permitted to use tax allocation accounting for timing differences between capital cost allowances and depreciation, the Company has not provided for deferred income taxes of $1,474,000 for the year ended December 31, 1978 (1977 – $1,653,000). The cumulative amount of deferred income taxes not provided for to December 31, 1978 is estimated to be approximately $14,200,000.

8. Other Income

Other income includes interest charged to construction of $327,615 (1977 – $292,815) less miscellaneous income charges. The interest charged to construction is also included in the item "Charges to construction not requiring an outlay of funds" in the Statement of Changes in Financial Position.

9. Pensions

The Company has a non-contributory plan which provides for service pensions based on length of service and rates of pay. The last actuarial review of December 31, 1975 indicated that all vested benefits were fully funded.

10. Remuneration of Directors and Officers

During the year 1978 the Company was served by 11 directors (1977 – 10 directors). As such their aggregate remuneration from the Company was $27,800 (1977 – $22,000).

The Company had 6 officers during 1978 (1977 – 6 officers) and their aggregate remuneration as officers was $238,074 (1977 – $225,312). Two of the officers served also as directors of the Company, one of whom received no director's fee.

11. Commitments

Material contractual obligations in respect of long term leases covering circuits, equipment and building space amounted to approximately $4,085,400 at December 31, 1978 (1977 – $2,859,300). The estimated minimum amount payable during the five years subsequent to December 31, 1978 is $2,593,500 (1977 – $1,786,500). Rentals incurred for the year ended December 31, 1978 amounted to $2,985,800 (1977 – $2,979,800).

12. Anti-Inflation Legislation

The Company is subject to the Federal Government's Anti-Inflation Legislation which became effective October 14, 1975 and was terminated on December 31, 1978. The Board of Commissioners regulates prices and profits for the Company under such legislation and prescribes guidelines for determining apparent excess income of the Company. Under these guidelines the Company had excess income of $943,175 net of income tax for 1978 and in accordance with Board Order No. 33, (1978) the amount was set aside in an account designated "Deferred Income Account" and deducted from net income for the year. Accordingly, the Board of Commissioners has approved a plan whereby any excess earnings at year end will be carried forward as earned income into fiscal year 1979.

Management is of the opinion that the Company is in compliance with the statute and current regulations.

13. Subsequent Event

The Company and Iron Ore Company of Canada have agreed to the purchase by the Company of the telephone plant and certain other assets comprising Iron Ore Company of Canada's telecommunication system in Labrador, Newfoundland, for a total purchase price of approximately $5,700,000. This transaction will be subject to the approval of such regulatory bodies or commissions as have jurisdiction.

Auditors' Report

To the Shareholders,
Newfoundland Telephone Company Limited.

We have examined the balance sheet of Newfoundland Telephone Company Limited as at December 31, 1978 and the statements of income, retained earnings and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these financial statements present fairly the financial position of the Company as at December 31, 1978 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Touche Ross & Co.
Chartered Accountants.

St. John's, Newfoundland.
February 8, 1979.

Ten Year Statistical Record

		1978	1977	1976
Telephone Service Facts				
Number of telephones		175,312	164,193	158,614
Percent dial	%	100	100	100
Local calls – daily average		2,993,425	2,869,614	2,643,948
Long distance calls – daily average		40,438	35,711	32,633
Income				
Total operating revenues	$	70,506,777	60,171,003	51,670,959
Other income	$	668,103	291,269	675,030
Operating expenses, transfer and taxes*	$	52,839,444	44,289,646	37,846,054
Interest charges	$	8,488,798	7,591,806	7,721,220
Net income before extraordinary items*	$	9,846,638	8,580,820	6,778,715
Extraordinary items	$	–	–	–
Net income*	$	9,846,638	8,580,820	6,778,715
Selected Balance Sheet Items				
Investment in plant and equipment	$	234,345,123	212,817,180	192,159,215
Total long term debt	$	85,771,941	91,767,941	83,113,941
Shareholders' equity*	$	86,485,088	71,947,165	59,579,985
Financial Ratios				
Earnings per average common share*	$	1.17	1.06	0.96
Dividends paid per common share	$	0.65	0.60	0.575
Equity per common share*	$	8.36	7.60	7.19
Percent long term debt to total capitalization	%	49.79	56.1	58.2
Rate of return on average total capital*	%	11.16	10.92	10.74
Interest in percent of average debt	%	9.56	8.68	9.38
Times interest earned before taxes		3.10	3.23	2.78
Other Statistics				
Construction expenditures	$	27,334,446	29,758,135	27,076,108
Plant investment per telephone	$	1,337	1,296	1,211
Number of employees		1,475	1,349	1,347
Salaries and wages paid	$	20,193,089	17,712,335	15,936,727

*Results reflect
(1) Tax payable basis for 1969 to 1972
(2) Partial tax allocation basis for 1973 to 1978

1975	1974	1973	1972	1971	1970	1969
150,389	142,058	123,157	109,829	100,664	92,991	88,247
100	99	99	97	97	96	95
2,145,158	1,949,919	1,690,456	1,516,542	1,290,705	1,108,248	979,179
30,395	26,052	20,594	17,534	15,068	14,384	13,562
42,884,148	35,398,838	26,177,774	22,207,582	19,174,109	17,450,266	13,261,627
630,611	726,289	167,799	52,861	58,379	84,394	31,655
31,258,307	25,796,798	19,646,744	15,701,200	13,489,574	12,909,281	10,271,669
7,106,774	5,599,005	2,845,919	2,399,889	2,209,441	2,035,149	1,876,109
5,149,678	4,729,324	3,852,910	4,159,354	3,533,473	2,590,230	1,145,504
–	–	–	–	–	1,113,850	355,181
5,149,678	4,729,324	3,852,910	4,159,354	3,533,473	3,704,080	1,500,685
169,422,806	146,343,959	94,182,627	79,419,848	70,020,022	62,475,742	55,379,535
81,600,941	75,244,941	43,804,000	30,802,000	30,659,000	25,841,000	24,526,500
49,211,108	39,052,563	37,341,772	36,480,242	30,175,472	28,954,427	23,733,468
0.83	0.86	0.69	0.80	0.70	0.80	0.37
0.50	0.50	0.50	0.50	0.45	0.41	0.40
7.02	6.74	6.38	6.19	5.94	5.70	5.34
62.4	65.8	54.0	45.8	50.4	47.2	50.8
10.15	10.54	9.01	10.24	9.93	11.14	7.25
9.06	9.41	7.63	7.81	7.82	8.08	7.68
2.38	2.57	3.81	3.54	3.23	4.84	3.03
27,323,473	28,614,346	16,243,036	10,610,682	8,642,025	8,044,828	6,514,027
1,127	1,030	765	723	696	672	628
1,278	1,324	1,124	953	877	824	849
13,583,388	10,763,803	7,787,214	6,216,497	5,284,000	4,632,144	4,073,949

Corporate Information

Head Office

Newfoundland Telephone Company Limited
343 Duckworth Street
St. John's, Newfoundland
A1C 5H6

1979 Annual General Meeting

The Annual General Meeting of Shareholders will take place at 10:00 A.M., Newfoundland Standard Time, Wednesday, March 28, 1979, in the Fort William Room, Hotel Newfoundland, Cavendish Square, St. John's, Newfoundland.

Listing of Common Stock

Newfoundland Telephone Company Limited common stock is listed on The Toronto and Montreal Stock Exchanges.

Registrar for Common Stock, Preferred Stock and Bonds, and Trustee for Bonds

Montreal Trust Company
253 Duckworth Street
St. John's, Newfoundland

Transfer Offices for Common Stock

Montreal Trust Company – St. John's, Halifax, Montreal, Toronto, Winnipeg, Regina, Calgary and Vancouver.

Transfer Offices for Preferred Stock and Bonds

Montreal Trust Company – St. John's, Halifax, Montreal, Toronto, Winnipeg, Calgary and Vancouver.

Directors

L.H.M. Ayre
Chairman, Ayre & Sons, Limited
St. John's, Newfoundland

A.A. Brait
President and Chief Executive Officer
Newfoundland Telephone Company Limited
St. John's, Newfoundland

D.W. Clark
President and General Manager
Bowater Newfoundland Limited
Corner Brook, Newfoundland

H. Collingwood
Chairman and President
Baine Johnston & Co. Ltd.
St. John's, Newfoundland

J.H. Farrell
Vice-President – Regulatory Matters
Bell Canada
Ottawa, Ontario

G.L. Henthorn
Vice-President and Comptroller
Bell Canada
Montreal, Quebec

H.L. Lake
Executive Vice-President
The Lake Group Limited
St. John's, Newfoundland

A.R. Lundrigan
President, Lundrigans Limited
Corner Brook, Newfoundland

D.D. Munro
Resident General Manager
Price (Nfld.) Pulp & Paper Limited
Grand Falls, Newfoundland

The Hon. F. O'Dea, Q.C.
Senior Partner
O'Dea, Greene, Puddester & Greene
St. John's, Newfoundland

F.J. O'Leary
Special Advisor to the Minister of Housing
Government of Newfoundland and Labrador
St. John's, Newfoundland

Officers

L.H.M. Ayre
Chairman of the Board

A.A. Brait
President and Chief Executive Officer

D.G. Wright
Director-Finance

R.H. Montgomery
Director-Planning

R.H. Benson
Comptroller

K.A.A. Marshall
Secretary-Treasurer

1978 Year in Review

An employee tests telephone lines in one of the Company's Central Offices.

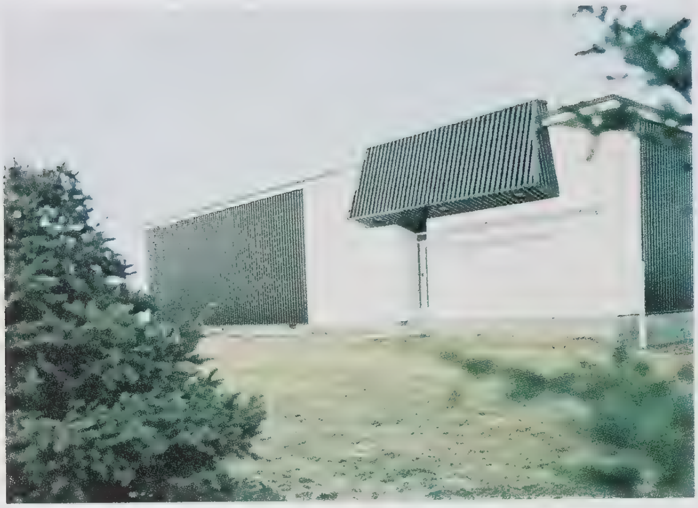
The CBC's television and AM/FM radio systems were brought onto the Company's microwave network during the year.

In 1978 the Company introduced Omnidata, Newfoundland's first provincial data network service.

Construction personnel faced challenges of varying weather conditions during the Labrador Improvement Program which was completed this year.

Phonecentre offers a wide variety of modern products for our customers.

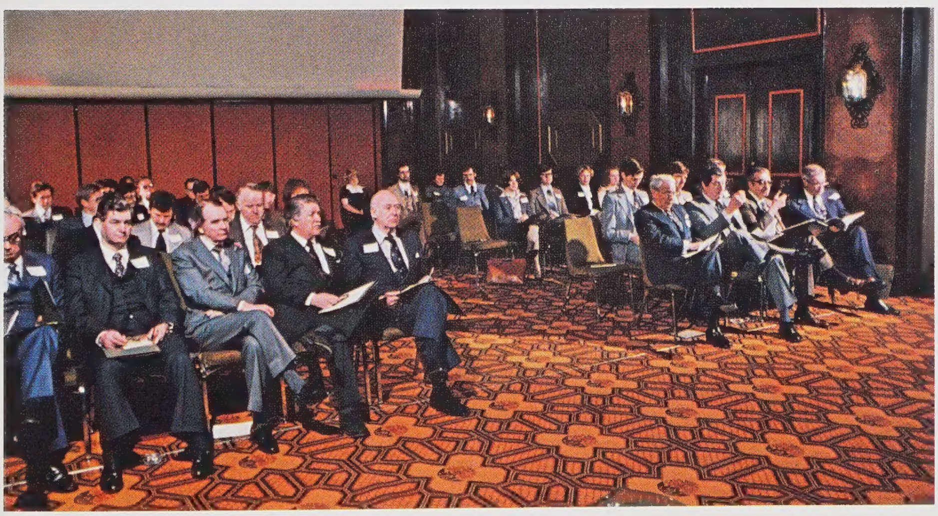
During the year the Company purchased the overseas cable terminal building located at Clarenville.



Our
Mount Pearl
exchange building
near St. John's
was expanded
during the year
to house a new
electronic
switching
machine.

Construction
of our new
Grand Falls
Central Office
building
was completed
during the
year.

A series of informational meetings was held with the investment community prior to our common share issue in October.



The 1978 Annual General Meeting of Shareholders was held in St John's on March 29, 1978.

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